

Money laundering in and through Australia, 2004

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By its nature, money laundering is unlikely ever to be measured accurately, but estimates of its cost to the economy can be made using a range of data sources. This research updates estimates of the cost of money laundering undertaken in 1995 and identifies risk areas for money laundering in and through Australia. It confirms that fraud constitutes the greatest source of laundered funds, followed by the illegal drug trade. The sectors that survey respondents identified as most likely to be utilised to launder money were banking, casinos, real estate and accounting. The mechanisms identified as most commonly used to launder money were cash and wire transfers, credit cards and 'payable through' accounts. There was also occasional use of gold and precious metals, and cheques. The respondents identified real estate, further criminal activities, gambling, luxury goods and legitimate business as the most likely activities in which the laundered money was invested. Taking several different methods of estimating losses from money laundering into account, the total estimate for 2004 was \$4.5b. While Australia's mature controls over national and international financial transactions place it at the lower end of the range of costs, the changing international financial environment and increasing sophistication of offenders mean that opportunities for new ways of money laundering continue to develop. Its potential to fund terrorist activities makes its identification and control even more pressing.

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Director

The 1995 report, *Estimates of the extent of money laundering in and through Australia* (Walker 1995) suggested that around \$3.5b per annum were believed to be generated by crime in Australia and laundered either in Australia or elsewhere, with the bulk generated by fraud and then drugs. This went against the prevailing international consensus, which was that the majority of laundered money was generated by drug offences. Since then, however, research around the world has increasingly identified fraud as the predominant international generator of criminal profits (compare, for example, the ACFE (2006) estimate of US\$638b for fraud with the ONDCP (2003) estimate of US\$64.8b on drugs).

A number of issues, such as the changing nature of crime, the factors that facilitate crime such as technology, the rise of terrorism, and the passage of time, presented the opportunity and need to revisit the earlier work, to assess whether Australia's response to money laundering more than a decade on continued to be effective and commensurate with the seriousness of the problem. It was also an opportunity to extend the analysis of the extent of money laundering to an assessment of the linkages of crime and money laundering in the Asia Pacific region, and to terrorism in the region.

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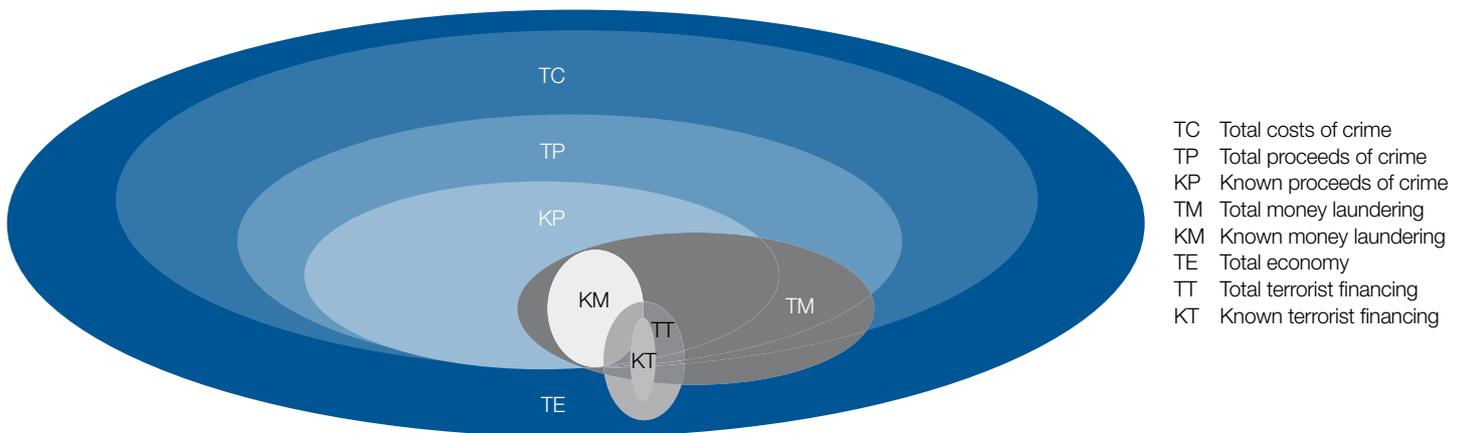
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Figure 1: Conceptual model of the economic relationships between crime, money laundering and terrorist financing



Note: The costs of crime are part of the Australian economy. The proceeds of crime are a subset of the costs. Some of the proceeds of crime in Australia are laundered, but some laundered money also comes from outside the Australian economy. Terrorist finance may not have criminal origins and is not necessarily laundered. The 'known' components are very small subsets of their respective estimated totals [not drawn to scale]

Worldwide concerns over the extent of money laundering, coupled with evidence that major terrorist activities have been facilitated by money laundering techniques, have significantly increased the level of knowledge and interest in money laundering. Understanding money laundering demands analysis of the size of the problem and its impacts on society. However, few real advances have been made in the quantification of money laundering at the regional or global levels. There is much reliance on former International Monetary Fund Managing Director Michel Camdessus' frequently quoted estimate of two to five percent of global GDP (Camdessus 1988), but there is little evidence of the basis of this estimate.

Apportioned to Australia these top-down estimates, would equate to about \$10.9 to \$27.3b in 1995 terms, far in excess of the Walker estimation of \$3.5b (using 2002–03 figures, the Camdessus estimate would suggest a range of \$14.7–36.7b). This shortfall suggests that Australia's relatively robust financial sector, the investment made in law enforcement and financial intelligence, and the nature of Australia's borders and stability have contributed to a lower than global average extent of laundering.

The recent research, conducted by John Walker Crimes Trends Analysis, RMIT University, and AUSTRAC, was based

on questionnaires and empirical data. It found that the extent of money laundering in and through Australia was not significantly different from that in 1995. However, law enforcement agencies are now much more successful in seizing large quantities of drugs and identifying corrupt business practices, partly as a result of access to AUSTRAC's financial intelligence.

This research built on the methodology of the 1995 report, again involving surveys of Australian law enforcement officials, and extending the survey to cover overseas financial intelligence units (FIUs), and researchers in Australia and overseas.

Methodology

The 1995 Walker report provided a definition of money laundering which graphically represented the relationship between costs of crime, proceeds of crime and money laundering. The expanded focus of the 2004 study to cover the financing of terrorism necessitated a review of this construct, to include elements of the legitimate economy. The revised construct appears in Figure 1.

The approach asked questions regarding:

- the main crime types and their significance
- the amount of proceeds/profit generated from these crimes
- how the proceeds were laundered

- where the funds were laundered
- the impact of laundering on society
- terrorism financing.

The study utilised:

- a survey of expert groups: law enforcement agencies; researchers and criminologists; and FIUs
- review of relevant annual reports and examination of AUSTRAC's database (financial transactions etc.)
- a review of relevant literature post-1995, including responses to the 1995 Walker report.

The survey

The study's objectives and the greater availability of information about money laundering suggested a wider survey than the 1995 one, which was only conducted within Australia. In particular, the growth since 1995 in the global network of FIUs offered the possibility of obtaining an overseas perspective of laundering in and through Australia. The scope of the questionnaire was also widened to include questions relating to laundering methods, trends, and links to organised crime and terrorism.

Accordingly, a range of survey documents were formulated, to cater for each of the expert groups. Altogether, the researchers

received 39 responses: 21 from overseas FIUs, 14 from Australian law enforcement agencies, and four from researchers and criminologists.

Responses from Australia

An estimate of \$3.8b for the total proceeds of crime generated by all crime types (TP in Figure 1) was derived from the Australian survey responses. Offences involving fraud and illicit drug trafficking again headed the list of crimes generating income for laundering, but when the amounts of money involved were compared, fraud exceeded drug crime by a significant margin. The best estimate for drug proceeds was \$382m (considerably less than the estimate in the 1995 Walker report) while frauds collectively totalled \$3.16b. Respondents estimated that on average over 80 percent of drug proceeds, and around 70 percent of the proceeds of fraud were laundered. The estimates of proceeds of crime and estimates of the percentages being laundered were combined to provide an estimate of the total amount of \$2.8b laundered (TM in Figure 1), either within Australia or overseas, from the proceeds of Australian crime. Fraud at around \$2.3b was by far the largest component of money generated and laundered in Australia; illicit drugs were second, at around \$300m.

By contrast, the total value of laundered money involved in cases actually proceeded against was likely to be in the order of only \$83m, and no data were available for the value of convictions recorded. However, the Australian law enforcement response was reported to have resulted in around \$100m in restrained proceeds of crime, and over \$21m forfeited. Illicit drugs to the street value of around \$1b were seized, along with real estate to the value of \$45m and \$40m in cash.

The banking sector, casinos, the real estate market and the accountancy profession were most commonly believed by survey respondents to be utilised for money laundering in Australia, sending money overseas or receiving it from overseas.

While the country most frequently cited in respect of money laundering was an Asian country, countries from almost all major world regions appeared in the list. Some of these are major trading partners of Australia, and/or have large expatriate or migrant communities in Australia. Perhaps surprisingly, the traditional tax havens and offshore centres in the Caribbean were not mentioned. Respondents distinguished clearly between countries where proceeds of crime were believed to be generated for laundering in or through Australia, those through which laundered money moved to a final destination, and countries regarded as final destinations of laundered money generated in Australia.

The research found that money laundering to, from, or within Australia was characterised by the frequent use of structuring transactions to avoid reporting requirements, accounts in false names, and cash smuggling. It is likely that launderers frequently used cash and wire transfers to effect money laundering involving Australia. The use of credit cards, 'payable through' accounts, and other electronic payments was not unusual. They occasionally used gold and precious metals, cheques and other instruments. The use of stored value cards was not frequent.

The estimated \$2.8b laundered in Australia was believed to be invested in a range of activities, including, as best estimates:

- 23 percent (\$651m) in real estate investment
- 21 percent (\$600m) in further crime activities
- 16 percent (\$449m) in gambling
- 15 percent (\$424m) in luxury goods
- 12 percent (\$345m) in legitimate business
- 7 percent (\$191m) in professional services.

Responses from overseas

As in Australia, overseas respondents mentioned fraud and drug crime most frequently as generators of criminal

proceeds. Motor vehicle theft and prostitution were ranked higher in overseas countries than in Australia, perhaps reflecting that Australia's water boundaries and distance from other countries offer some protection against offences of this type, which involve the physical transportation of vehicles or people across national borders. The counterpoint to this is that computer crime, which crosses borders without impediment, was of more concern to Australian law enforcement agencies than to the overseas respondents.

The survey of overseas FIUs asked about the relative frequency of suspected offence types in suspect transaction reports. Various forms of fraud and tax/customs evasion were mentioned over four times as often as drug trafficking. Other types of offence were much more rarely the subject of suspicious transaction reports. Countries differ substantially in the extent to which different crimes generate proceeds that may be laundered. In some countries, crime types including frauds, illegal prostitution and people trafficking, resulted in a very high percentage (80–90%) of the proceeds of crimes being laundered. Money launderers in other countries appeared more likely than their Australian counterparts to spend their money on lifestyle investments, professional services and corrupt or improper influences, and less likely to spend it on real estate investment and gambling.

Reflecting the global nature of the survey's respondents, a wide range of countries were seen as linked to money laundering in one way or another; the most frequently mentioned were north American, European and southeast Asian countries. Eastern European countries were most frequently named as countries where the proceeds of crime were generated, northern and central European countries were associated with transit operations, while southeast Asia was mentioned most in connection with destinations of laundered money.

None of the respondents regarded Australia as significant in any area of their own money laundering environment, although

some believed Australia was of moderate significance as an origin country, and others saw Australia as of moderate significance as a destination of laundered funds from their country. The responses to the survey suggested that either there was a net flow of money laundering out of Australia, or the avenues by which laundered funds flow back to Australia were not sufficiently visible to authorities.

None of the overseas respondents identified any terrorist financing links between Australia and their country. Their assessment of potential sources of terrorist funding was similar to that of Australian observers, in that they ranked donations ahead of crime and legitimate business. Legitimate business was, however, more likely to be highly ranked than in Australia.

Other approaches

Costs-of-crime-based estimation

The 1995 Walker analysis commenced with estimates of the costs of crime, applying percentages to derive estimates of the proceeds of crime, and then the amount likely to be laundered. The percentages of costs estimated to accrue to the offender in the form of proceeds, and the percentages of proceeds laundered were derived in 1995 by consensus among Australian criminologists.

Mayhew (2003) subsequently updated estimates of the costs of crime in Australia in 2001–02, documenting the likely property losses from each crime type. For most crime types considered in Mayhew's costs of crime estimates, the property losses represented the proceeds of crime to the offender. For drug crime, however, Mayhew incorporated other social costs, not related to the proceeds of crime accruing to the offender. Estimates of the proceeds of drug crime in Australia can, however, be derived from recent United Nations Office on Drugs and Crime (UNODC 2005) estimates of the value of illicit drugs trades around the world in 2002–03.

These data can be combined with AUSTRAC's 2004 survey-based estimates of the percentages laundered to give an alternative estimate of money laundering generated by crime in Australia. The resulting figure is around \$6.3b, equally shared between fraud and drug offences. The difference between the survey-based estimates and these costs-of-crime-based estimates is largely in their perceptions of the profitability of the illicit drug trade in Australia, and may be at least partially due to the different dates of the estimates. Successes by Australian law enforcement in intercepting illicit drugs and breaking up trafficking networks may have significantly reduced the laundered proceeds of illicit drugs crime between 2002–03 and 2004–05.

Suspicious transaction estimates

AUSTRAC's own data (2007) on suspect transactions (SUSTRs) show that most unusual financial behaviour is reported by the banking and gaming sectors. By value, however, while financial institutions are still the highest reporting dealer type, the next highest type is the insurance, bullion, and securities and futures broker sector. The two most common suspected behaviours suggested by these reports were tax evasion and structuring transactions to avoid mandatory reporting obligations.

The trends show increases in both the numbers and values of SUSTRs, but it is difficult to know to what extent the increases were indicative of the widening scope of the legislation, improving accuracy in identifying suspicious transactions, or actual increases in numbers of transactions where a suspicion was aroused. It is also difficult to ascertain the extent, if any, to which reporting institutions are over-reporting suspicious transactions (defensive reporting), to avoid criticism by authorities.

While the face values of SUSTRs have increased over time, it must be recognised that these values may:

- over-represent the level of suspicious behaviour, as no actual offence might have occurred in relation to a particular disclosure, or
- under-represent, in that the report is only made for that part of the subject's behaviour which has come to the notice of the particular institution at that time.

Of the \$123.5b total face value of SUSTRs in 2003–04, \$122.4b related to a small number, each of which had a face value in excess of \$100m and were unlikely to have actually been completed.

Analysis of international funds transfers

Analysis of international funds transfer instruction reports would, on the face of it, be a very useful means of identifying money laundering flows in and out of Australia. If illicit drugs payments, for example, were significant enough to become identifiable in the data, it would be expected that more money would be sent to drug producer countries than is received from them. The data showed no such relationship. Similarly, analysis of flows to and from known tax havens neither conclusively pointed to money laundering between particular countries nor suggested how much of the flow of funds between countries was laundered proceeds of crime.

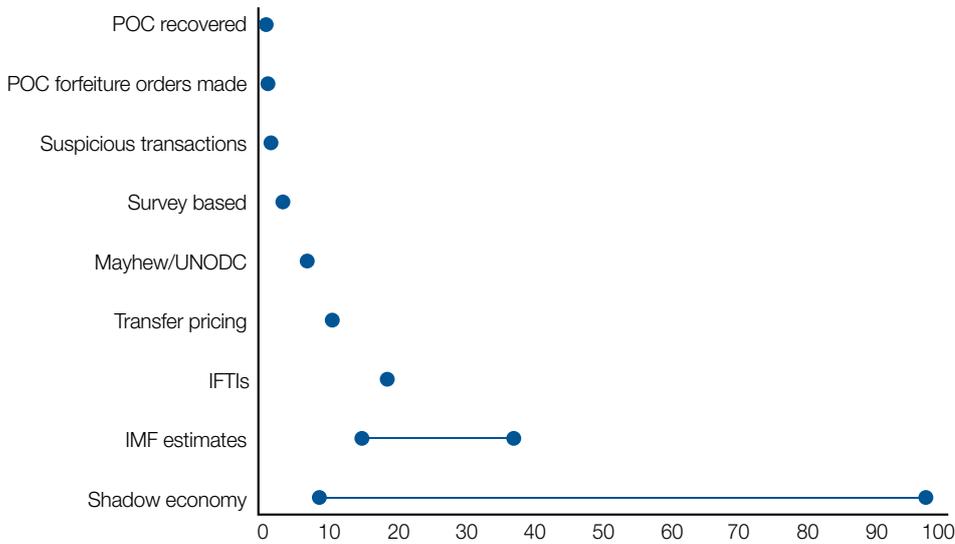
Estimates of the shadow economy

The Australian Bureau of Statistics (2003) estimated that an adjustment to GDP figures for 2000–01 to reflect the extent of the underground economy was warranted, in the order of 1.3 percent, or \$8.4b. By contrast, Schneider (2004) estimated that the Australian shadow economy could be in the order of 13.5 percent of GDP.

Trade pricing anomalies

Zdanowicz (2003) studied trade pricing anomalies involving the United States and other countries. He concluded that transfer pricing, where a business falsely under- or over-states the value of an export or import, is a highly effective

Figure 2: Estimates of money laundered in and through Australia (\$b)



way to launder money. Zdanowicz found anomalous trade between the US and Australia, in the order of US\$1.84b (7% of total trade between the two countries).

Proceeds of crime recoveries

Some of the proceeds of crime in Australia are clearly identified in data on prosecutions under the *Proceeds of Crime Act 2002*. Statistics from the Australian Federal Police (2004) indicate an annual average of orders made over the period 1999–2000 to 2003–04 in the region of \$30.9m, with recoveries averaging \$8.6m.

These figures, however, are clearly not measuring the totality of either the proceeds of crime or money laundering in and through Australia. The Commonwealth Director of Public Prosecutions (2004: 39) suggested that:

the amount recovered can not be the sole measure of the effectiveness of the legislation. The true test is whether the Act is operating to punish and deter crime and to disrupt criminal enterprises.

What these estimates show

While the survey estimates were based on considerable local knowledge of Australia and the major crimes that come to official notice, they may have underestimated the

extent or the profits of crimes that never come to public notice, including both fraud and drug crimes, particularly as they were based on a small number of respondents to the survey. The approach using the work of Mayhew and the UNODC specifically addressed estimates of unrecorded crime, and may be less susceptible to that type of error, but relied on much higher estimates of the profitability of the illicit drug markets in Australia. An assessment of the various estimates, however, leads to a conclusion that crime in Australia in 2004 generated between \$2.8b and \$6.3b, with the most likely figure being in the vicinity of \$4.5b.

Although this is well below the likely Australian component of the IMF figure of two to five percent of global GDP, the analyses also identified significant areas of hard-to-quantify shadow economy and transfer pricing practices that may involve significant underpayment of tax. Practices like these can be used by Australian launderers or by overseas launderers seeking to launder money through Australia. They could increase the total money laundered in and through Australia considerably. For Australia, two to five percent of GDP would suggest a figure between \$14.7 and \$36.7b laundered in 2002–03. Research was not able to determine

the components that constitute this IMF figure, making Australian comparisons extremely difficult. That is, does it just relate to drugs, fraud and other criminal offences, or does it include factors such as the shadow economy and transfer pricing? It also raises the question as to the relevant proportion for Australia, with its robust economy and financial sector. Would Australia be at the lower end of a scale, perhaps falling well below the lower bound of two percent of GDP?

The values of other statistical aggregates, including suspect transaction reports, international funds transfer instructions and proceeds of crime orders, can only be a guide to the actual extent of money laundering.

Impacts of money laundering on the economy

Survey respondents and other information suggested that launderers generally invested their proceeds of crime into real estate or other sterile assets such as high value luxury items. If a figure of \$4.5b is taken as the value of money laundering in Australia, and that of this, approximately 23 percent is invested into real estate, nearly \$1b is reallocated from other sectors (that is, the normal consumption of victims and drug users) to real estate. The ownership of dwellings sector yields the lowest economic benefits for each dollar invested in the sector of all sectors, in terms of output, income, imports and employment. It is therefore possible to consider the economic multiplier effects of this reallocation, in terms of the changes to economic output, demand for level of income, imports, and employment. For each \$1m reallocated to real estate, there could be average net losses to the economy of around \$1.436m in output, \$576,000 in income and 20 jobs.

The launderer’s need to launder funds can also result in distortive effects on the prices of investments such as real estate, because the need to find a safe investment is more important than price.

Launderers may also seek to legitimise their earnings by mingling illicit funds with proceeds from legitimate businesses

(generally those with high cash turnover). Again, this method of laundering is often done at any cost, even to the extent of operating a business at a loss and subsidising its business operations with contributions from criminal earnings. This exerts downwards pressures on prices, and tends to crowd out legitimate business competitors.

Further, money laundering has wider implications for the economy, including:

- the risk of corruption to institutions and some entire financial sectors
- losses to the financial and government sectors are recovered from the community in the forms of higher prices for their services
- misleading monetary data changes in savings patterns.

The financing of terrorism

It is generally accepted that some of the main methods utilised by the financiers of terrorism include the misuse of charities, the informal funds transfer sector, wire transfers, and precious and durable commodities. Other methods can include trade mispricing, and intellectual property crime (Noble 2003). Very little is known about amounts of terrorist financing, and there is some risk in assuming that a person who is the subject of a SUSTR is the same person named on government-proscribed lists. The simple match of a name does not of itself mean that the reported person is linked to the financing of terrorism. The research suggests that it would be naïve to assume that no funds used for the financing of terrorism had originated in Australia. However, the survey

responses provided no conclusive evidence of terrorist financing in Australia or in the region.

Further research

The study identified some areas of further research, particularly a consideration of trade values compared with funds transfers, and the possible use of alternative payment technologies for money laundering. Other work could explore the extent of trade mispricing involving Australia. The greatest need, however, is for internationally comparable data on the proceeds of crime and money laundering. This requires a consistent method that can be adopted widely.

Acknowledgment

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